INFORMED BUDGETEER

THE BILL ARRIVES: FINAL SCORING OF TEA 21

- The President signed the Transportation Equity Act for the 21st Century (TEA 21) on June 9, 1998. Final scoring of the Act became available this week (see table below).

Enacted TEA-21
Discretionary Caps and Mandatory Spending Offsets
(Outlays in Billions)

	1999	2000	2001	2002	2003	Total[A]
CBO WODI[B]	26.25	26.95	27.41	27.43	27.73	135.8
New Transp. Caps	26.29	29.20	31.39	32.69	33.98	153.5
Highways	21.89	24.44	26.20	26.98	27.73	127.2
Mass Transit	4.40	4.76	5.19	5.71	6.26	26.32
Net changes-Discretionary	0.04	2.25	3.98	5.25	6.25	17.34
Mandatory Offsets						
Veterans benefits[C]	-0.48	-1.02	-1.96	-5.93	-5.97	-15.4
Student Loans[D]	0.05	--	--	--	--	0.09
SSBG & TANF	--	--	-0.63	-0.68	-0.96	-2.26
Aquatic Resources Fund	--	--	--	--	0.01	0.01
Net Mandatory spending[E]	-0.43	-1.02	-2.59	-6.61	-6.92	-17.5
TEA 21 receipt changes	0.03	0.01	0.03	0.07	0.07	0.21
Budgetary Impact (98-03)	-0.37	1.24	1.43	-1.28	-0.60	0.02

[A]Total includes 1998 impact.
[B]FY 2003 level inflated.
[C]OMB scoring of veterans provision is net of enacted TEA 21 and House-passed Technical Corrections Bill.
[D]Non-Probablistic scoring.
[E] With OMB estimates for veterans benefits.

- The scoring above reflects the enacted version of TEA 21. The TEA 21 Technical Corrections bill, which the House passed on June 3 by voice vote, will make changes to the veterans provisions in TEA 21. Those veterans changes are reflected in the table above.

- The bottom line? Passage of TEA 21 is essentially offset-- all but $20 million. When TEA 21 was passed by Congress on May 22, it was believed that the bill had offsets that totaled $200 million more than necessary (*Bulletin* # 14).

- Th reason for this change is that the Joint Committee on Taxation (JTC) scored a $200 million revenue loss between '99 and '03 for TEA 21.

- Even with these changes, *Bulletin* readers can still take heart. TEA 21 is on-budget, still discretionary spending, and its spending increases are essentially offset.

TEA-21'S HIGHWAY AND TRANSIT "FIREWALLS"

- Want to know how Congress will make darn sure highway programs, transit programs, and the roughly 2,100 earmarked transportation projects in the Transportation Equity Act for the Twenty-first Century (TEA-21) get funded? The answer is in subtitle A of title VIII of TEA-21, which amended the Balanced Budget and Emergency Deficit Control Act to create two new "firewalls" on highway and transit spending.

- What's a "firewall"? The Balanced Budget Act of 1997 extended through 2002 the discretionary spending limits, or caps, on annually appropriated funds. That law also established separate limits on defense, nondefense, and violent crime reduction discretionary funding for 1999. These separate spending limits, or firewalls, effectively segregate a specified amount of annually appropriated spending for defense and violent crime reduction from all other discretionary funding.

- Highways and transit spending are considered nondefense discretionary spending and must compete with other programs under the nondefense discretionary cap. While the Senate took tough votes to offset the additional spending for the highway bill with reductions in specific direct spending programs, the House punted. They took highways off-budget.

- Off-budget was unacceptable. Instead, the conference report on TEA-21 included reductions in direct spending to offset its additional highway and transit spending. It also segregated discretionary funding exclusively for highways and transit programs by establishing two new discretionary limits for highways and transit that are similar to the current defense and violent crime limits with a couple of exceptions.

- Unlike the hard spending caps on defense or crime funding, TEA-21 included a special rule that provides that any spending in excess of the highway and transit limits be charged to the nondefense discretionary spending limits. Next, TEA-21 provided two adjustments to the highway and transit outlay limits.

- One of TEA-21's key objectives was to ensure that highway gas taxes would be spent. To meet this objective, the first adjustment requires OMB to adjust the highway outlay limit for fluctuations in gasoline tax levels. TEA-21's highway spending levels and the highway outlay limits are based on CBO's February 1998 estimates of tax receipts to the highway trust fund. To the extent actual revenue levels differ from these 1998 estimates or OMB's updated estimates for the budget year is different than these 1998 estimates, OMB is required to adjust highway obligation levels in TEA-21 by that amount. Next, OMB is required to calculate the outlay changes that would result from the change in the obligation levels and adjust the highway outlay limits by that amount.

- The second adjustment is to make sure that highway and transit spending would be held harmless for technical outlay re-estimates. Under this second adjustment, OMB is required to take a snapshot of the cost of TEA-21 by making an estimate of the outlays that would result from TEA-21 in its final sequester report due this fall. Each year, as part of the President's budget submission, OMB is required to update its estimate of the outlays resulting from TEA-21, compare this revised estimate of TEA-21's outlays to the snapshot taken in the 1998 final sequester report, and adjust the outlay limits by the difference.

- Although TEA-21 provided dramatic increases in transportation spending, it paid for 98.5% of this additional spending, kept this spending on-budget, and continued to subject these programs to the appropriations process. It also took the complexity of the budget process to new heights and gave new meaning to the term outlay limit -- at least with respect to highway and transit spending.

LINE ITEM VETO RULED UNCONSTITUTIONAL

- On Thursday, June 25, 1998, the Supreme Court issued its opinion in the Line Item Veto cases and by a 6-3 margin held that the Act is unconstitutional because it violates the Presentment Clause (Article I, section 7) of the Constitution.

- Justice Stevens wrote the opinion for the Court in which he was joined by Rhenquist, Kennedy, Souter, Thomas and Ginsberg. The Court found that both the New York and the Snake River appellees had standing to challenge the Line Item Veto. With respect to both the New York and Snake River appellees, the Court found that they did have standing.

- The Court then went on to find the Line Item Veto Act unconstitutional because it violates the procedures established in Article I, section 7 - the Presentment Clause. Because the Court found one constitutional violation sufficient, it declined to address the Separation of Powers/delegation issue also raised by both groups of appellees.

- In short, the Court felt that the Line Item Veto Act had both the legal and practical effect of permitting the President to unilaterally amend both the Balanced Budget Act of 1997 and the Taxpayer Relief Act of 1997 by repealing a portion of each law.

- The Court specifically rejected the Government's two arguments that the Line Item Veto Act was analogous to : (1) the authority granted to the President to suspend certain tariffs established by the Tariff Act of 1890; and (2) the long history of Congress in appropriating sums which the President may decline to spend in whole or in part.

- With respect to the Tariff Act of 1890, the Court felt that the Line Item Veto was clearly different in that the Tariff Act allowed the President to suspend the exemption of tariffs on a *limited list* of goods contained in that Act only upon the occurrence of a specific subsequent contingency (a country producing those same goods had imposed a tariff upon our goods). In contrast, the Line Item Veto permits the President to cancel any of the spending or tax items before him (assuming they satisfy the definitions in the Line Item Veto Act) without any *specific* limitation or contingency.

- The Court seemed to focus upon the fact that the Tariff Act *required the President to act* if and when certain actions were taken by other countries; whereas the Line Item Veto Act *permits the President* to cancel spending if, in his opinion, certain criteria are met. The Court was very concerned that this permits the President to take action fulfilling his own policy preferences, as opposed to executing a duly enacted law upon a *subsequent change* in circumstances.

- The Court summarily dismissed the long history of Presidents declining to spend in whole or in part certain appropriations, by declaring that the specific terms of these laws themselves granted the President discretion with respect to amounts to be spent and how funds would be allocated. It felt that Line Item Veto on the other hand, gives the President “the unilateral power to change the text of duly enacted statutes”.

- Interestingly, the Court did address the “lockbox” issue which arose during the oral arguments. (See *Bulletin* # 11) However the Court dismissed the Government’s argument and focused upon the fact that with respect to the appellees, the law had now changed - they would no longer benefit from the language as intended by Congress. The fact that the law would be given some effect with respect to the Federal Government’s budget - deficit reduction - in no way lessened the fact that the law had been changed with respect to the intended beneficiaries.

ECONOMICS

THE GROWING DISCREPANCY

- All levels of government have been surprised by the exceptionally high level of revenue inflows over the last few years. It is interesting to ask why this has been the case.

- One partial hypothesis is that GDP may have understated true economic activity over the last few years. Since revenue projections are built upon assumptions of multi-year GDP growth, understated GDP would lead to understated revenue projections. Such thoughts stem from the growing divergence between product-based output measures (GDP) and income-based output measures (Gross Domestic Income or GDI).

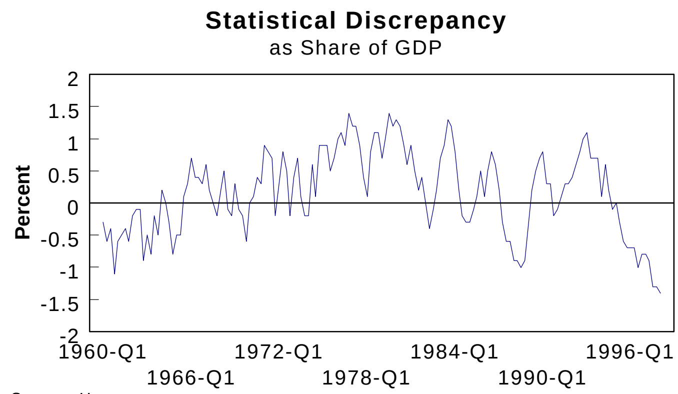
- Since GDP and GDI are theoretically measuring the same concept, they should be equal over time. However, short-term deviations do arise due to measurement difficulties. The difference between GDP and GDI is called the statistical discrepancy or stat. As noted above, the stat should average to zero over time.

- In a somewhat unusual pattern, however, the stat has trended steadily lower since the start of 1993, thus inflating GDI relative to GDP. In fact, GDI has grown 0.5 percentage points faster than GDP in each year since 1993.

- Some speculate that GDI may be giving us a better picture of the economy at present, since 1) it is more consistent with recent revenue growth and 2) it is possible that GDP is having increasing difficulty picking up growth in the rapidly expanding (but hard to measure) service sector.

- Nonetheless, we should be careful not to jump to an immediate conclusion regarding the GDP/GDI question, particularly since GDP has historically been a more reliable measure of activity than GDI.

- The issue does warrant further technical investigation, however. The Bureau of Economic Analysis (which produces the national accounts data) is studying the issue closely and has crafted a thoughtful proposal to improve the source data for GDP measures. Such an initiative should enhance the accuracy of our statistics, yielding benefits for budget forecasters and policy makers.



Source: Haver

BUDGET QUIZ

QUESTION: Where did Treasury get the dollars it sold during its foreign exchange intervention on June 17th? What impact does it have on the federal budget?

ANSWER: From the Exchange Stabilization Fund (ESF).

The Treasury appears to have sold $417 million dollars on June 17th, and bought an equivalent amount of yen. (The Federal Reserve is assumed to have sold an equal amount of dollars as well, although this won’t be known definitely for a while longer).

The Treasury’s share of the intervention dollars were held by the ESF and invested in nonmarketable Treasury securities. Since the ESF had to redeem these securities to raise the intervention dollars, the US gross debt would have fallen by $417 million due to this transaction. There is no net interest saving from the redemption itself, however, since the government would just be reducing interest payments made to itself.

However, there is still an impact on the federal budget. When the ESF redeemed its Treasury holdings, the cash dollars it received had to come from somewhere. In this case, we’ll assume that they came from Treasury’s cash bank deposits where they would have been earning roughly 5.50 percent. After the intervention, these proceeds are now denominated in yen and held in yen assets which pay less than 1 percent interest. This will reduce the government’s interest earnings from what they otherwise would have been and thus will have a very tiny negative impact on yearly budget totals.

There is another potential budgetary channel as well -- since the yen fluctuates in value constantly, there could be a trading loss or profit on our holdings of foreign currency. However, for simplicity, we do not consider this here.